FILE COPY

Office Supreme
JAN
CHARLES

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1931

---

No. 639

---

L. J. BLAKEY (Successor to R. E. Schumacher), Receiver of the First National Bank of New Bern, New Bern, North Carolina, Petitioner,

*vs.*

CHARLES J. BRINSON, Respondent.

---

**PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT.**

---

J. O. CARR,
JULIUS F. DUNCAN,
GEORGE P. BARSE,
*Attorneys for Petitioner.*

## INDEX.

### Subject Index.


| | Page |
|---|---|
| Petition: | |
| I. Summary of matters involved | 2 |
| II. Reasons for granting the writ | 4 |
| Brief in support of petition: | |
| I. Opinions below | 9 |
| II. Jurisdiction | 9 |
| III. Statement of case | 10 |
| IV. Specification of errors | 10 |
| V. Summary of argument | 11 |
| VI. Argument | 12 |
| A. The necessary elements of a preferred claim, and the rule stated as to augmentation and tracing | 12 |
| B. The appropriation of a deposit or credit balance does not result in augmentation but merely in a shifting of bookkeeping credits | 16 |
| C. There was no augmentation of assets, or tracing to the receiver, in the instant case | 18 |
| D. There was no valid basis for attempting to impress the cash in the bank with a trust based upon the transaction with Brinson and the bookkeeping credits resulting therefrom in his favor | 21 |
| E. Breach of trust by the bank cannot, of itself, constitute a basis for a preferred claim | 24 |
| VII. Conclusion | 25 |


### Citations.


| Cases: | |
|---|---|
| American Can Company vs. Williams, 178 Fed. 420 | 6, 16 |
| Beard vs. Independent District of Pella City, 88 F. 375, 382, 383 | 5, 16 |
| Blumenfeld vs. Bank, 38 Fed. (2) 455 | 6, 16 |
| Brennan vs. Tillinghast, 201 Fed. 609, 612, 613 | 6, 16 |
| Cunningham, Trustee of Ponzi, vs. Brown, 265 U. S. 1, 11 | 5, 16, 22, 25 |
| Davis vs. McNair, 48 Fed. (2) 494 | 7, 22 |

Page

Empire State Surety Company vs. Carroll County, 194 F. 593, 604, 605, 606 ..... 5, 13, 25
Hirning vs. Federal Reserve Bank, 52 Fed. (2) 382 ..... 5, 16, 17
Jenkins, Receiver, vs. National Surety Company, 277 U. S. 264 ..... 8
Larabee Flour Mills vs. First National Bank, 13 Fed. (2) 330, 331 ..... 5, 16
Schuyler vs. Littlefield, 282 U. S. 707, 710, 713 ..... 5, 16, 22, 24
St. Louis & S. F. R. R. vs. Spiller, 274 U. S. 304, 310. 5, 16, 22, 25
Titlow vs. McCormick, 236 Fed. 209, 211, 212 ..... 6, 16

Statutes:

Section 240 (a), Judicial Code (U. S. C., Title 28, Sec. 347). 10
Section 5236, United States Revised Statutes ..... 12

# SUPREME COURT OF THE UNITED STATES.

## OCTOBER TERM, 1931

---

## No.

---

L. J. BLAKEY (Successor to R. E. Schumacher), Receiver of the First National Bank of New Bern, New Bern, North Carolina, Petitioner,

*vs.*

CHARLES J. BRINSON, Respondent.

---

## PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT.

---

Your petitioner, L. J. Blakey, as Receiver of the First National Bank of New Bern, New Bern, North Carolina, prays that a writ of certiorari issue to review the decree of the United States Circuit Court of Appeals for the Fourth Circuit, rendered in the above case (R. 37).

After the argument of the case in the Circuit Court of Appeals, and prior to the decision thereof, peti-

tioner, L. J. Blakey, succeeded R. E. Schumacher as Receiver of the said First National Bank of New Bern, by virtue of an appointment by the Comptroller of the Currency of the United States, and hence files this petition as such successor.

## I.

### Summary of Matters Involved.

The United States District Court for the Eastern District of North Carolina rendered judgment (R. 25) allowing respondent, Charles J. Brinson, a preferred claim against the cash in said First National Bank of New Bern at its suspension. The receiver of the suspended bank appealed to the Circuit Court of Appeals, and the judgment of the District Court was affirmed, and petitioner now seeks a review of the decree of the Circuit Court of Appeals.

On October 14, 1929, respondent Brinson had a deposit balance of $1,961.31 in the First National Bank of New Bern, and on that date deposited therein the further sum of $2,100, said additional deposit being in the form of a check drawn upon the Eastern Bank & Trust Company of New Bern, North Carolina, thereby making his deposit balance $4,061.31 (R. 10, 12, 18, 19). At the time of the deposit the bank agreed to buy for Brinson United States Government bonds of a par value of $4,000, with the understanding that the purchase price thereof was to be charged against his deposit account. The aforesaid deposit of $2,100 was made by Brinson for the specific purpose of building up his deposit balance so as to enable it to be used

in the purchase of the bonds (R. 10-13). On October 19th the bank advised Brinson that the bonds had been bought for him (which was untrue) and a memorandum of a charge to his account of the contemplated purchase price of the bonds in the sum of $3,964.60 was given him. The actual charge against the account was made on October 21st, and on the same date the bank's "bond account" was credited with the sum of $3,964.60 (R. 12-14-18). For some reason not explained by the record, the bonds were not actually ordered for nor delivered to Brinson and had not been ordered up to the time of suspension of the bank on October 25, 1929. At all times between October 14th and the date of suspension of the bank, there was actual cash in the vaults of the bank in excess of the sum of $3,964.60, the supposed purchase price of the bonds (R. 19-20).

The aforesaid check of $2,100 on the Eastern Bank & Trust Company was forwarded to that bank, with other items, and the clearing balance between the two banks was in favor of the First National Bank to the extent of $5,801.09 (R. 20), and the First National Bank received in payment drafts in the sum of $5,801.09 upon the Norfolk National Bank of Commerce & Trusts, which drafts were forwarded to the Norfolk Bank for credit of the First National Bank. Said credit was entirely dissipated through drafts upon the Norfolk Bank issued by the First National Bank and by subsequent disbursements from the account so that at the close of business on October 25th the First National Bank had not only exhausted its balance with the Norfolk Bank, but had incurred an overdraft of $970.20 (R. 20-23), the result being that the receiver of the

suspended bank acquired no portion of the proceeds of the original check of $2,100 at the time he took over the assets of the suspended bank (R. 22).

After due demand on the Receiver, Brinson brought suit for allowance in the sum of $3,964,60 of a preferred claim or lien upon the cash taken over by the Receiver (R. 3). The Receiver defended on the ground that the proceeds of the deposit account of Brinson had not augmented or increased the bank's assets, and that no funds or property belonging to the plaintiff could be traced to the cash taken over by the receiver at suspension (R. 24). The District Court held that there had been augmentation of assets of the bank and tracing of the deposit account to the cash in the hands of the receiver and that a preferred claim should be allowed. The Circuit Court of Appeals also held that there was augmentation, but that irrespective of augmentation the cash in the bank at the time of the transaction was impressed with a trust for the full amount of the supposed purchase price of the bonds, and thereupon affirmed the judgment of the District Court and allowed the preferred claim.

## II.

## Reasons for Granting the Writ.

THE FACTS IN THE CASE ARE NOT IN DISPUTE. PETITIONER COMPLAINS OF THE CONSTRUCTION OF SAID FACTS AS A MATTER OF LAW WHEREIN IT WAS HELD:

(1) That augmentation of assets and tracing to the receiver existed, and

(2) That irrespective of augmentation and tracing a preferred claim was proper by reason of the cash in the bank being impressed with a trust in favor of the plaintiff.

Petitioner feels that writ of certiorari should be granted because:

(*a*) The decision and decree of the Circuit Court of Appeals involves a Federal question relating to the rights of creditors against national banks under the National Banking Laws, and the decision of the Circuit Court of Appeals appears to be in conflict with the principles of law established in analogous cases by this Honorable Court. *Schuyler* v. *Littlefield,* 232 U. S. 707, 710, 713; *Cunningham, Trustee of Ponzi,* v. *Brown,* 265 U. S. 1, 11; *St. Louis & S. F. R. R.* v. *Spiller,* 274 U. S. 304, 310.

(*b*) The decision of the Circuit Court of Appeals is in conflict with the principles of law established by the decisions of the Circuit Courts of Appeal in analogous cases in other circuits, namely:

Eighth Circuit:

*Larabee Flour Mills* v. *First National Bank,* 13 F. (2) 330, 331.

*Beard* v. *Independent District of Pella City,* 88 F. 375, 382, 383.

*Empire State Surety Co.* v. *Carroll County,* 194 F. 593, 604, 605, 606.

*Hirning* v. *Federal Reserve Bank,* 52 Fed (2) 382.

Sixth Circuit:

*Brennan* v. *Tillinghast*, 201 Fed. 609, 612, 613.

Ninth Circuit:

*Titlow* v. *McCormick*, 236 Fed. 209, 211, 212.

Tenth Circuit:

*Blumenfeld* v. *Bank*, 38 Fed. (2) 455.

Second Circuit:

*American Can Company* v. *Williams*, 178 Fed. 420.

The foregoing cases in the various circuits, and the decisions of this Honorable Court, above cited, establish the principles of law *that a preferred claim can be allowed against the estate of an insolvent only where* (1) the transaction with the preferred claimant resulted in augmentation or increase of the assets of the insolvent by the property of the claimant or the proceeds thereof in the form of actual cash or other tangible assets (as distinguished from the establishment and appropriation or dissipation of a deposit or book credit) and (2) that such property or assets of the preferred claimant, or other property identified as being in lieu thereof, can be traced into the hands of the receiver or trustee taking over the assets of the insolvent at the time of suspension or bankruptcy, and (3) that the burden of showing the facts of augmentation and tracing is upon the preferred claimant and that the law will not presume augmentation and tracing. Assuming such principles of law to be controlling in the establishment of preferred claims, it would appear that the decision of the Circuit Court of Appeals is

clearly contrary to such principles for the reasons that augmentation and tracing did not exist in the instant case, and the court was in error in its construction of the principles of law relating to augmentation and tracing and also in holding, as a matter of law, that a preferred claim existed regardless of augmentation.

(*c*) The Circuit Court of Appeals has decided an important question of general law relating to insolvent estates, in a way probably untenable and in conflict with the weight of authority indicated by the foregoing decisions.

(*d*) The precise kind of case decided by the Circuit Court of Appeals has not, apparently, heretofore been passed upon by this Court. Since the decision of the Circuit Court of Appeals in this case and since the decision of the Circuit Court of Appeals for the Fifth Circuit in the somewhat similar case of *Davis* v. *McNair*, 48 Fed. (2) 494 (relied upon by the Circuit Court of Appeals in the instant case), a considerable number of cases have arisen in the districts covered by these circuits, and the District Courts apparently have no alternative but to follow the decisions of the Circuit Courts of Appeal in the Fourth and Fifth Circuits, and the indications are that if the principles established by the decision in the instant case are permitted to stand, the basis and scope of claims against insolvent national banks in receivership will be very substantially broadened, and a considerable number and amount of claims will have to be allowed, to the detriment of the general creditors. The Comptroller of the Currency is charged with the liquidation of hundreds of in-

solvent national banks throughout the country, and consequently it is important that the questions of law involved in the instant case be determined by this Honorable Court so that the policy of the Comptroller's office in such administration may be uniform in application in the various circuits of the several circuit courts of appeal of the United States. It is felt that in the interest of establishing uniformity in the various circuits, this Honorable Court should pass upon the questions of law in issue in the instant case, just as was done, for the same reason, in the case of *Jenkins, Receiver,* v. *National Surety Co.,* 277 U. S. 264.

WHEREFORE it is respectfully prayed that the petition for writ of certiorari be granted.

J. O. CARR,
JULIUS F. DUNCAN,
GEORGE P. BARSE,
*Attorneys for Petitioner.*

# SUPREME COURT OF THE UNITED STATES.

## OCTOBER TERM, 1931

---

## No. -

---

L. J. BLAKEY (Successor to R. E. Schumacher), Receiver of the First National Bank of New Bern, New Bern, North Carolina, Petitioner,

*vs.*

CHARLES J. BRINSON, Respondent

---

## BRIEF IN SUPPORT OF PETITION.

### I.

### Opinions Below.

The opinion of the Circuit Court of Appeals is reported in 52 Fed. (2) 821, and appears in the Record at pages 32-37. Judgment of the United States District Court appears in the Record at pages 25-26.

### II.

### Jurisdiction.

The decree of the Circuit Court of Appeals was entered October 17, 1931 (R. 37). Jurisdiction is con-

ferred upon this court to review this cause by writ of certiorari under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925 (U. S. C. Title 28, Section 347).

## III.

### Statement of Case.

A statement of the case is set out in the foregoing petition under the caption "Summary of Matters Involved," to which reference is here made. Such elaboration of the facts as appears to be pertinent and necessary to the discussion will be indicated where appropriate.

## IV.

### Specification of Errors.

(a) The Circuit Court of Appeals held that upon the facts stated the transaction of the plaintiff with the insolvent bank resulted in augmentation of the assets of the bank. This was error for the reason that according to the undisputed facts the respondent Brinson established a deposit balance and this deposit balance was transferred as a matter of bookkeeping from his account to the bond account of the bank and no new funds came into the bank as a result thereof. The proceeds of the $2,100 check included in the deposit did not result in augmentation of the bank's assets, but the credit therefrom resulting in the correspondent of the suspended bank was entirely dissipated before suspension, and no assets came into the hands of the receiver from said check.

(*b*) The Circuit Court of Appeals held that irrespective of augmentation and tracing, the cash in bank at the time of the transaction of respondent Brinson with the bank was impressed with a trust in his favor in the sum of $3,964.60, the anticipated purchase price of the bonds, and that a preference claim should be allowed. This was error for the reasons that (1) a preferred claim cannot properly be allowed against an insolvent estate unless there is augmentation of assets and a tracing of those assets or the proceeds thereof to the receiver or trustee taking over the estate of the insolvent; (2) the bank had no funds belonging to the plaintiff, but only a credit balance in his favor arising out of the relationship of debtor and creditor between the bank and its depositor, and (3) the cash in the bank was not the cash of the depositor Brinson but the property of the bank, and no part thereof was segregated, or intended to be segregated, for the use of the plaintiff, and the credit balance upon the books in favor of Brinson could not properly be traced into the cash of the bank.

## V.

## SUMMARY OF ARGUMENT.

A preferred claim against a national bank can exist only where the transaction of the claimant with the bank has resulted in a relationship of trust between the bank and the claimant, and where, in addition, the assets of the bank have been augmented or increased by new cash or property accruing from the claimant, and where said funds or property can actu-

ally be traced to the assets taken over by the receiver of the bank at suspension. No augmentation and tracing occurs where the transaction results only in the appropriation or use of a deposit or credit balance, the same constituting, in such case, merely a shifting of bookkeeping credits, and no tracing exists where, assuming augmentation, the proceeds of augmentation are entirely dissipated or disbursed prior to suspension of the bank. No augmentation or tracing existed in the instant case, and there was merely a shifting of credits from the deposit account of Brinson to the bond account of the bank, and there was no basis for attempting to impress the cash in the bank with a trust based upon the bookkeeping credits.

## VI.

## ARGUMENT.

### A. The necessary elements of a preferred claim, and the rule stated as to augmentation and tracing.

Section 5236 United States Revised Statutes, relating to insolvent national banks in receivership, contemplates that the assets thereof shall be distributed pro rata among all of the creditors and claimants. No provision is made in the National Banking Laws for preferred claims. The Courts have, however, established a basis for preferred claims where the claimant can show that the receiver has, among the assets, identifiable property belonging to the claimant. In working out the formula or procedure for establishing such claims, the Federal Courts have held generally that the claimant must show, by the burden of

proof, that from the transaction of the claimant with the bank before suspension the bank received property of the claimant in trust, that the property so received actually augmented the existing assets of the bank by way of adding thereto cash or other property (as distinguished from the addition of a bookkeeping credit) and that the augmented assets, or the proceeds thereof, are traceable into the assets taken over by the receiver. If for example a bank receives an item for collection, and collection is made in the form of cash (as distinguished from the receipt in payment of a check drawn upon the bank) or if a bank receives cash funds in trust for a specific purpose, it is considered that a trust relationship exists in such cases, and that the existing assets of the bank have been augmented or increased by the trust property, and consequently if it can be shown further that said trust property was not dissipated by the bank prior to suspension, but on the contrary the trust funds, or other funds constructively in lieu thereof, were retained by the bank and were taken over by the receiver at suspension, a preferred claim will be allowed. This rule is summarized in the decision of the Circuit Court of Appeals for the Eighth Circuit in *Empire State Surety Company* vs. *Carroll County*, 194 Fed. 593, 603, 604, 606. In that case the bank had improperly received deposits and had fraudulently represented that it was solvent. In stating the applicable principles of law concerning preferred claims, the Court said:

> "This is a suit in equity against the receiver of a national bank to require him to take from the ratable dividends of other creditors of the

bank the requisite amount to pay the county's claim in full. The receiver must make the distribution of the property of this bank in accordance with the provisions of the national banking law. It is the dominant purpose and requirement of that law that, after provision for a redemption of its notes is made, the proceeds of an insolvent national bank shall be equally distributed among its unsecured creditors. So imperative is this provision that it repeals a former act of Congress giving a preference to the United States and annuls a statute of a state giving a preference to deposits of savings banks. Rev. St. sec. 5236 (U. S. Comp. St. 1901, p. 3508); *Davis* v. *Elmira Savings Bank,* 161 U. S. 275, 285, 16 Sup. Ct. 502, 40 L. Ed. 700. *National Bank* v. *Colby,* 21 Wall. 609, 613, 614, 22 L. Ed. 687. The burden, therefore, is on the sureties to prove clearly that they are entitled on equitable principles to the preference they seek. They proved that the bank took the deposits of the county and of its other depositors in trust for them respectively. But this was not enough. They were also required to prove that these deposits or their proceeds, or a certain part of them, came to the hands of the receiver, for he is liable to *cestuis que trustent* to pay trust funds in full only to the extent that he receives them.

* * * * * * *

"It is indispensable to the maintenance by a *cestui que* trust of a claim to preferential payment by a receiver out of the proceeds of the estate of an insolvent that clear proof be made that the trust property or its proceeds went into a specific fund or into a specific identified

piece of property which came to the hands of the receiver, and then the claim can be sustained to that fund or property only and only to the extent that the trust property or its proceeds went into it. It is not sufficient to prove that the trust property or its proceeds went into the general assets of the insolvent estate and increased the amount and the value thereof which came to the hands of the receiver.

* * * * * * *

"But checks of third persons on the bank with which they are deposited which are paid by crediting the bank and charging the drawers on its books fail to increase the cash in its possession and form no basis for a preferential payment to the depositor. *Beard* v. *Independent District of Pella City*, 88 Fed. 375, 382, 31 C. C. A. 562.

"Moreover, the deposit of checks of third persons which are credited to the depositor and used by the bank to pay its debts bring no money into its fund of cash and form no foundation for preferential payment to the depositor. *City Bank* v. *Blackmore*, 75 Fed. 771, 773, 21 C. C. A. 514.

"Again, checks of third parties deposited with a bank credited to the depositor and collected through a clearing house lay no foundation for a preferential payment, in the absence of proof of the actual balance of cash the bank received on account of them, for they may have been and usually are used in whole or in part to discharge the debts of the bank. In re Seven Corners Bank, 58 Minn. 5, 59 N. W. 633; *City of St. Paul* v. *Seymour*, 71 Minn. 303, 308, 74

N. W. 136; *Willoughby* v. *Weinberger*, 15 Okla. 226, 229, 79 Pac. 777.

To the same effect see:

Eighth Circuit:

*Larabee Flour Mills* v. *First National Bank*, 13 Fed. (2) 330, 331;

*Beard* v. *Independent District of Pella City*, 88 Fed. 375, 382, 383;

*Hirning* v. *Federal Reserve Bank*, 52 Fed. (2) 382.

Sixth Circuit:

*Brennan* v. *Tillinghast*, 201 Fed. 609, 612, 613.

Ninth Circuit:

*Titlow* v. *McCormick*, 236 Fed. 209, 211, 212.

Tenth Circuit:

*Blumenfeld* v. *Bank*, 38 Fed. (2) 455.

Second Circuit:

*American Can Company* v. *Williams*, 178 Fed. 420.

Also see *Schuyler* v. *Littlefield*, 232 U. S. 707, 710, 713; *Cunningham, Trustee of Ponzi* v. *Brown*, 265 U. S. 1, 11; *St. Louis & S. F. R. R.* v. *Spiller*, 274 U. S. 304, 310.

**B. The appropriation of a deposit or credit balance does not result in augmentation but merely in a shifting of bookkeeping credits.**

The Federal Courts have held generally that the shifting or appropriation of a deposit or credit balance

in a bank, whereby such shifted deposit or credit balance accrues to the bank, either as trustee or otherwise, contributes no additional assets, and creates no additional fund in the bank, and that consequently augmentation of existing assets does not occur. This situation frequently arises where an item has been forwarded to a bank for collection against one of its depositors, and the bank receives in trust in payment of the item a check of the debtor drawn upon his deposit account. In such case a charge is made to the debtor's deposit balance, and a corresponding credit, for remittance purposes, is made in favor of the owner of the item. In such case no new funds accrue to the bank, and there has been merely a shifting of bookkeeping credits, and consequently there has been no augmentation. Under such circumstances a preferred claim cannot be allowed, according to the Federal decisions. In a very recent case in the Eighth Circuit of *Hirning* v. *Federal Reserve Bank*, 52 Fed. (2) 382, the Court, in discussing these principles, said:

> "It is contended by the appellee that the checks sent by the Reserve Bank to the Brookings Bank *constituted a trust fund*, and that this trust fund has been traced into the currency and collection items sent by the Brookings Bank to the Reserve Bank.
>
> The trial court seems to have adopted this view as one of the grounds of its decision in ordering judgment for defendant.

*We do not agree with this contention.* It must be remembered that the checks sent to the Brookings Bank by the Reserve Bank were all of them checks drawn on the Brookings Bank. When the Brookings Bank accepted the checks, this produced no additional funds in its hands. Its assets were not augmented. *No trust fund was created.* If there was no trust fund, there could, of course, be no tracing of the trust fund into any assets of the Brookings Bank. The doctrine that a trust fund is created when checks drawn on bank A by a depositor therein are sent to bank A by bank B for collection, i. e., for payment, has been disapproved by the decisions in this Circuit, as has also the doctrine that the forwarding bank or its principal has a general lien on the assets of the drawee bank for the payment of such checks. *Rorebeck* v. *Benedict, etc. Co.*, 26 Fed. (2) 440; *Farmers National Bank* v. *Pribble*, 15 Fed. (2) 175; *Larabee Flour Mills* v. *First Nat. Bank*, 13 F. (2) 330; *Macy* v. *Roedenbeck*, 227 Fed. 346, 352; *Beard* v. *Independent Dist.*, 88 Fed. 375."

(Italics inserted.)

To the same effect are the cases in the various Circuits cited in paragraph A next preceding.

C. **There was no augmentation of assets, or tracing to the receiver, in the instant case.**

In the instant case the respondent Brinson had an existing deposit balance of $1,961.31 in the First National Bank of New Bern. He deposited, in regular course in his account, a check for $2,100 drawn on the Eastern Bank and Trust Company and received credit therefor, with the understanding that the bank would purchase approximately $4,000 of Liberty Bonds and

charge his account for the amount thereof when purchased. In the meantime the deposit was to stand to his credit for the full amount. It will be noted that the agreement between the parties contemplated the use of the deposit balance at a future date in the same manner as if at such future date the depositor had drawn a check to the bank for the amount of the contemplated purchase price of the bonds. The situation is, therefore, exactly analogous to the cases cited and quoted, *supra*, where a depositor gives his bank a check on his account in payment of an obligation. As already indicated, no new assets are added to the bank by such transaction, and a shifting of credits or bookkeeping entries only results. In the instant case the bank charged the deposit account of Brinson with $3,964.60 (the contemplated purchase price of the bonds), and credited its bond account with a corresponding amount, thereby shifting the credit from the deposit account of Brinson to the bond account of the bank in trust for Brinson. The assets of the bank, however, were no greater before, than after, the shifting of the deposit credit.

The $2,100 check drawn on the Eastern Bank & Trust Company should, under elementary principles, be considered to have been the property of the bank in that it was deposited in the account of Brinson in the customary manner (R. 19), and although it was expected that the credit thereby resulting would be used in the future for the purchase of bonds, nevertheless in the meantime it stood to his credit and the proceeds should be considered the property of the bank. Assuming, however, for discussion only (but

not conceding), that the $2,100 check must be treated as trust funds, it will be noted that no augmentation of assets of the bank occurred, and no tracing of the proceeds to the receiver can be established. As explained in the summary of facts, *supra*, the clearing of the item, with other items, between the First National Bank and the Eastern Bank & Trust Company, resulted in a balance in favor of the First National Bank of $5,801.09, for which the First National Bank received drafts on a Norfolk bank. The drafts were transmitted to the Norfolk bank for credit of the First National Bank with other items aggregating $11,908.88 (R. 21) and an examination of the account of the Norfolk bank with the First National Bank (R. 22) discloses that although the balance on October 14 was $10,226.12 in favor of the First National Bank, the balance on October 15, after the deposit of the items aggregating $11,908.88 was only $9,413.61, that is to say, the balance in the Norfolk bank after such deposit was, by virtue of withdrawals, less than the balance on October 14. Thereafter successive withdrawals from the account by the First National Bank resulted in an overdraft on October 18 of $5,810.56, thereby conclusively showing that the $2,100 item, included in the item of $5,801.09, which in turn was included in the item of $11,908.88 was entirely dissipated by October 18, so that it is obvious from the record that no part of the proceeds of the $2,100 check could have been taken over by the receiver. As a matter of fact, at the close of business October 25, the account (R. 22) still showed an overdraft against the First National Bank of $970.20.

It seems obvious from the foregoing that the conclusions, as a matter of law, of the Trial Court, and of the Court of Appeals, upon the undisputed facts, that augmentation of assets occurred, was error. Indeed it is evident from the opinion of the Circuit Court of Appeals that not much importance was attached to the factor of augmentation so far as the deposit account or the $2,100 check were concerned, but, as next discussed, the Court held a preferred claim existed regardless of augmentation and tracing.

**D. There was no valid basis for attempting to impress the cash in the bank with a trust based upon the transaction with Brinson and the bookkeeping credits resulting therefrom in his favor.**

The court below held that irrespective of the factor of augmentation and tracing, the cash in the bank at the time of the transaction with Brinson was impressed with a trust in his favor to the amount necessary to purchase the bonds, and that consequently inasmuch as the bank thereafter at all times had on hand sufficient cash to equal the supposed purchase price of the bonds, a preferred claim existed.

The first reason assigned by the court is that the agreement of the bank to charge the account of Brinson with the purchase price of the bonds must be considered equivalent to the giving of a check by Brinson upon his account, and from this point the court proceeds further and holds that the giving of a check for such purpose and the charging of the same to the account, would have been the same in effect as cashing

the check and immediately giving back to the bank the cash funds to purchase the bonds, and that in such latter case there would be an augmentation of assets as the basis for a preferred claim. The position that the giving of a check by a depositor and the charging of the same to his account is, in legal effect, equivalent to the cashing of the check by the depositor and the delivery of the cash to the bank, is clearly contrary to the whole trend of decisions in the Federal courts other than in the fourth and fifth circuits (as previously noted), in that the other circuits unquestionably hold that the giving of a check by a depositor upon his account and the charging of his account therewith, amounts to no more than a shifting of bookkeeping credits and does not bring in any new cash or assets nor constitute the basis for a preferred claim.

The case of *Davis* v. *McNair,* 48 Fed. (2) 494, in the fifth circuit, and the State cases cited and quoted by the court below in support of this point (R. 34, 35) are, for the reasons hereinbefore stated, contrary to the general trend of the Federal cases established in the other circuits, and contrary to the principles relied upon by this Honorable Court in *Schuyler* v. *Littlefield,* 232 U. S. 707, 710, 711, 712, 713, and *Cunningham, Trustee of Ponzi* v. *Brown,* 265 U. S. 1, 11, and *St. Louis & S. F. R. R.* v. *Spiller,* 274 U. S. 304, 310.

A further basis assigned by the court below is to the effect that the claim of the respondent, Brinson, was not asserted on the ground that the assets of the bank had been augmented but upon

> "an agreement by the bank that a definite amount of the funds in its possession shall be

> held in trust for a specified purpose. In other words, what the record discloses is, not a shifting of credits, but the creation of a trust with respect to funds already in the bank's possession." (R. 36.)

In reply it may be pointed out, in the first place, that paragraph No. 10 of the bill of complaint filed in the District Court does rely upon augmentation (R. 6) and augmentation was an issue in the case (R. 24). In the second place it is to be noted that the record does not disclose an agreement by the bank that "a definite amount of the funds in its possession" shall be held in trust for a specified purpose, but on the contrary the undisputed facts disclose merely an agreement on the part of the bank to purchase the bonds, and when so purchased, to charge the account of the depositor with the price of the same. In the third place it is to be noted that what the record *does* disclose *is* "a shifting of credits", in that a portion of the deposit account or credit of Brinson is shifted to the bond account of the bank. The court points out further, however, that the bank, in charging Brinson's account, and crediting the bond account

> "paid to itself the money necessary for the purchase of the bonds, and charged itself with the same as trustee." (R. 36).

It is obvious that the bank did not, by these bookkeeping entries, pay itself any money, and that the action so taken was merely preliminary to, and in anticipation of, the purchase of the bonds.

**E. Breach of trust by the bank cannot, of itself, constitute a basis for a preferred claim.**

Assuming (for discussion only, but not conceding it) that the bank was guilty of breach of trust in failing to purchase the bonds, and was guilty of improper conduct in charging Brinson's deposit account and advising him that the bonds had been ordered when they had not been ordered, nevertheless, such misconduct cannot constitute the basis of a preferred claim if there does not coincide augmentation of assets from the transaction, and tracing of the proceeds in actual funds to the receiver. As a matter of fact most preferred claims are based upon some form of breach of trust. In the case of *Schuyler* v. *Littlefield, supra,* certain brokers obtained stock from the preferred claimant by fraudulent representations. The brokers sold the stock, and the owners attempted to establish a preferred claim against the bankruptcy estate of the brokers. In upholding the judgment of the lower court denying a preferred claim, this Honorable Court said as to the obligation upon the preferred claimant, as follows:

> "Like all other persons similarly situated, they were under the burden of proving their title. If they were unable to carry the burden of identifying the fund as representing the proceeds of their Interborough stock their claim must fail. If their evidence left the matter of identification in doubt the doubt must be resolved in favor of the trustee, who represents all of the creditors of Brown & Co., some of whom appear to have suffered in the same way.

Like them, the appellants must be remitted to the general fund."

To the same effect see *Cunningham, Trustee of Ponzi* v. *Brown, supra; St. Louis & S. F. R. R.* v. *Spiller, supra; Empire State Surety Company* v. *Carroll County, supra.*

## VII.

## CONCLUSION.

It is believed that the foregoing discussion demonstrates that the decision of the court below is contrary to the principles of law established in the circuit courts of appeal in the circuits other than the fourth and fifth circuits, and to the principles established by the decisions of this court. It is earnestly urged, in the interest not only of uniformity in the administration of national banks throughout all of the circuits, but also in the interest of settling conclusively what the law is upon the issues involved, that this court entertain a review of this case on writ of certiorari, and we submit, in the light of the reasons indicated, that the petition should be granted.

J. O. CARR,
JULIUS F. DUNCAN,
GEORGE P. BARSE,
*Attorneys for Receiver.*